STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on May 16, 2007

COMMISSIONERS PRESENT:

Patricia L. Acampora, Chairwoman
Maureen F. Harris
Robert E. Curry, Jr.
Cheryl A. Buley

CASE 03-C-0428 - Complaint of Phone Management Enterprises, Inc. and Other Pay Telephone Operators Against Verizon New York Inc. for Refunds Relating to Unlawful Underlying Payphone Service Rates.

CASE 03-C-0519 - Complaint of American Payphone Communications, Inc. Against Verizon New York Inc. Concerning Alleged Refunds Relating to Unlawful Underlying Payphone Service Rates.

ORDER DENYING REHEARING AND ADDRESSING COMMENTS

(Issued and Effective May 24, 2007)

BY THE COMMISSION:

INTRODUCTION AND SUMMARY

A previous order in these proceedings ("the Rate Order") revised the tariffed rates and charges that Verizon New York Inc. (Verizon, the company) collects from payphone service providers (PSPs, the complainants),[1] for public access lines (PALs) and related services through which the PSPs obtain access to the network.[2] As a result, four matters remain to be decided in today's order.

---

[1] In these proceedings, PSPs also have been referred to as independent payphone providers or IPPs.

[2] Cases 03-C-0428 and 03-C-0519, Order Resolving Complaints and Inviting Comments Regarding Public Access Line Rates (issued June 30, 2006). An extensive summary of the litigated issues and procedural history as of that date may be found in the Rate Order and in a Procedural Ruling by the Administrative Law Judge (issued January 14, 2005).

comments.[9] Upon review of the comments,[10] we determine in today's order that the PAL tariffs need not be modified to reflect cost offsets from access charge revenues, other than those offsets already incorporated in the new rates that Verizon has submitted in its July 31, 2006 compliance filing.

Fourth, the complainants' comments on Verizon's compliance filing propose two modifications of the new tariffs. One would provide for automatic adjustment of PAL rates to reflect any increase in access charges, and the other would address an asserted inconsistency among the tariffs' references to recognition of access charge revenues as a cost offset. Today's order adopts the first proposal to a limited extent, and declines to adopt the second.

PETITION FOR REHEARING

The complainants' petition for rehearing takes issue with four aspects of the Rate Order. However, as Verizon observes, each element of the petition fails to establish the legal or factual error required under 16 NYCRR 3.7(b) as a predicate for reconsideration.

Moreover, Verizon is correct that the complainants are misreading the Rate Order insofar as they construe it to mean we must either (a) indiscriminately apply all the cost inputs we adopted as part of our Total Element Long Run Incremental Cost (TELRIC) analysis when setting unbundled network element (UNE) rates in Case 98-C-1357 ("the UNE rate case"),[11] or (b) indiscriminately reexamine all the UNE rate case inputs for purposes of this case. On the contrary, as the Rate Order explains, the scope of our discretion is not confined to those two alternatives. A rational determination of PAL costs and

---

[9] Notice of Filing Dates and Conference (issued August 3, 2006).

[10] Letter to the Secretary from Keith J. Roland, Esq. on behalf of PSP members of Independent Payphone Association of New York, Inc., dated August 15, 2006; Verizon's and complainants' Initial Comments dated respectively August 11 and August 24, 2006; Verizon's Reply Comments dated September 5, 2006.

[11] N.Y. Telephone Co. - Rates, Order on Unbundled Network Element Rates (issued January 28, 2002).

for whom we set rates in the UNE rate case on the basis of a 5.9% overhead factor.[14]

Verizon points out that the complainants are incorrect in alleging a lack of cost evidence because, after the complainants initially made that allegation in their comments on the white paper, Verizon did in fact provide our advisory staff the calculation and work papers supporting the company's 10% estimate. And, more fundamentally, Verizon is correct that the affirmative justification needed to support "overhead allocations" under the second Wisconsin order inevitably entails the application of theories and judgment because overheads, by their very definition, are costs that cannot be allocated solely on the basis of empirical studies.[15] In this instance, the Rate Order properly adopted the 10% factor as a means of assigning PAL rates an overhead allocation comparable to that borne by other, comparably competitive services. The Rate Order's approach is fully consistent with the second Wisconsin order's requirement that overhead allocations be "justified," as well as with our broader obligation to set rates based on forward-looking cost estimates pursuant to the NST.

---

[14] Use of a 6.1% overhead factor is described as Proposal 4 at the conclusion of the complainants' petition. The complainants' Proposal 3 is that we "require Verizon's payphone rates to be calculated using [a] retail cost figure equivalent to that used for CLEC TELRIC rates." (Petition, p. 13.) We assume Proposal 3 is either a general request that we adopt without modification the cost inputs used in the UNE rate case (a point addressed elsewhere in today's order), or an allusion to the complainants' argument that we should recognize the PSP migration likely to result from increases in CLECs' PAL rates relative to Verizon's (as discussed in the accompanying text). Otherwise, complainants' Proposal 3 seems to have no antecedent in the text of their petition. Compare complainants' Comments on Staff White Paper, dated March 14, 2005, pp. 14-17.

[15] In a different context (the imputed ratio of Integrated Digital Loop Carrier and Universal Digital Loop Carrier deployment, discussed in the next section), the complainants themselves cite approvingly the Rate Order's statement that "it is not the use of actual data that renders a rate cost-based within the meaning of the NST; rather, what the NST requires is a forward-looking cost methodology." Rate Order, p. 21, quoted in complainants' petition at p. 5.

determination because Verizon provides PSPs no unbundled service offerings. Moreover, the complainants argue, a ratio that assumes some UDLC deployment will perversely reward Verizon for imprudently failing to optimize the efficiency of its PALs and other basic services while the company focuses its investment on competitive wireless and fiber optic services. The complainants also question the reliability of Verizon's planning assumptions incorporated in the 57%/43% ratio.

As Verizon observes, the complainants' arguments are simply unresponsive to the Rate Order insofar as it already has taken them into consideration. The complainants are correct that the uncertainties regarding service offerings to CLECs at the time of the UNE rate case are merely tangential to the Rate Order in these proceedings. However, that is not because we should be estimating loop costs specifically for PSPs that use no unbundled loops, as the complainants imply;[17] but because the Rate Order does not even use the 85%/15% ratio which had resulted from concerns about unbundled loops in the UNE case. As for the alleged suboptimality of a 57%/43% deployment, the Rate Order notes that the complainants have made no showing of imprudence, and their mere allegation of a bias favoring competitive services does not cure that deficiency. Moreover, the Rate Order explains that in this case we can effectively satisfy the NST's mandate of a forward-looking cost methodology by exercising our discretion to recognize the costs of both a maximally efficient "end state" network and the present network as it actually exists. That approach forecloses the complainants' proposed evidentiary standard--for which they provide no rationale, in any event--that any modification of the inputs adopted in the UNE rate case must be based on "irrefutable evidence that the assumptions made in [the UNE case] are compelled to be changed."[18] Finally, the

[17] The Rate Order rejected the theory that loop costs imposed by PSPs should be estimated separately from loop costs generally, because (as the Order observes in discussing loop growth rates) "any given loop can be used for PAL services or other purposes." Id., p. 16, note 16. The complainants' petition cites no error of fact or law in that approach.

[18] Complainants' petition, p. 6.

used for PAL service, to produce a 3% growth rate in loops overall.) By simply calling attention to those same circumstances again, the complainants present no persuasive reason to believe that the Rate Order has understated the loop growth rate.

Geographic Deaveraging

In the UNE rate case, to recognize that loop costs tend to be lower in urban areas than elsewhere, we estimated loop costs separately for each of three geographic zones: Zones 1A (Manhattan), 1B (major cities outside Manhattan), and 2 (all other). In these proceedings, the Rate Order accepted the white paper's presumption that PAL lines are distributed among the three zones in the same proportion as all Verizon's other loops, despite the complainants' allegation that the white paper's loop cost estimate was overstated insofar as PSPs use PAL lines predominantly in the two low-cost, urban zones (1A and 1B).

In the Rate Order, we questioned whether the complainants' proposal was useful or economically significant, because the PAL lines used by Verizon's own payphone service are concentrated in Zone 2 where they tend to negate the cost savings associated with the PSPs' lines in the urban zones. We also cited the complainants' obligation to address the customer impacts of their proposal, which, by imputing the low urban costs of Zones 1A and 1B to higher cost PAL lines in Zone 2, might impair the economic viability of Verizon's own non-urban payphone service in Zone 2.[22]

On exceptions, the complainants ask that we reconsider that decision on the ground that Verizon's own payphone operations in Zone 2 are being curtailed and may even be divested, thus eliminating our concern about recognition of relatively high loop costs in that zone. In opposition, Verizon says we should dismiss the complainants' argument because it already was considered in the Rate Order.

[22] Id., pp. 18-19.

including evidentiary support;[25] and that in deciding highly technical questions, we are not compelled to consider or ignore any particular factor or assign it some preordained weight.[26] For the reasons discussed above, complainants' petition presents only matters previously considered and addressed in the Rate Order, or other criticisms that fail to identify errors in that order. Accordingly, the petition is denied.

NST CRITERIA AND PRIOR RATES

We initiated these proceedings partly in response to a State Supreme Court directive that we determine whether the PAL rates antedating the Rate Order complied with the NST's requirement (as of April 15, 1997, the relevant date as determined by the Supreme Court) that rates reflect a forward-looking cost methodology.[27] On appeal, however, the Appellate Division had found that we need not order Verizon to pay refunds to PSPs, should we determine that the pre-existing rates had been excessive, i.e., not NST compliant. The Appellate Division based this conclusion on a letter to the FCC from representatives of Verizon's predecessor, requesting an extension of time in which to review existing rates and file new rates and proposing a refund in the event the new rates were indeed lower than existing rates.[28] The Rate Order noted that the Independent Payphone Association of New York, Inc. (IPANY, representing many of the complainants in these proceedings) subsequently had petitioned the FCC to determine, as an exercise of preemptive Federal jurisdiction, that noncompliance with the NST would necessitate

---

[25] Brief in Opposition, p. 3, citing Campo Corp. v. Feinberg, 279 A.D. 302, 307 (3d Dept. 1952), aff'd, 303 N.Y. 995 (1952).

[26] Id., pp. 3-4, citing, inter alia, N.Y. Tel. Co. v. PSC, 95 N.Y.2d 40, 48-49 (2000).

[27] IPANY v. PSC and Verizon, Albany Co. Index No. 413/02 (July 31, 2002). Complainants had sought refunds of any excess charges imposed from April 15, 1977 onward, because that was a deadline set by the FCC for implementation of NST compliant payphone rates.

[28] IPANY v. PSC and Verizon, 5 A.D.3d 960, 963-64 (3d Dept. 2004), app.den., 3 N.Y.3d 607 (2004).

we based the PAL rates at issue in the remand order. Verizon observes that those rates were established by decisions we issued in 2000 and 2001,[32] so that a review of past NST compliance not only would be purposeless but might pose the conundrum of having to estimate forward-looking costs retrospectively as of 2000 and 2001. On the other hand, Verizon suggests, we might discharge our obligations under the remand relatively simply, by clarifying to the Supreme Court's satisfaction how the existing record supports our previous representation to the Court that we had based the rates on forward-looking costs.

Verizon apparently believes that refunds conceivably remain an open issue, given the allegedly unlikely possibility that IPANY will prevail in its pending petition to the FCC.[33] Verizon nevertheless contends that the petition at the FCC provides no basis for additional proceedings in response to the Supreme Court's remand, because the remand concerns only compliance with federal law as of 1997 whereas any FCC decision on the IPANY petition would address compliance with subsequent FCC decisions (including the second Wisconsin Order) and would require initiation of new proceedings. Verizon concludes that any further investigation pursuant to the remand would be a wasted effort mandated neither by the courts nor, as yet, by the FCC, which would have to explain its rationale and intent before we could determine what further analysis we must perform to comply with the FCC's decision.

The complainants, meanwhile, argue that we should move forward with the remand proceeding. They claim that the FCC has the authority to set aside state PAL rates and that the FCC is likely to order refunds, based on the preemption theories advocated in IPANY's petition to the FCC. They further argue

---

[32] Cases 99-C-1684, IPANY - Petition for Rates and Refunds, and 96-C-1174, Coin Telephone Services, Order Approving Permanent Rates (issued October 12, 2000) and Order Denying Petition for Rehearing (issued September 21, 2001).

[33] Filed December 29, 2004 in CCB No. 96-128.

it considered forward-looking cost data and that Verizon's rates were based on that data, it cannot assert for the first time in this proceeding a different ground for its determination than what is expressed in its initial determination."[35] The Court accordingly concluded that "although the pre-existing PAL rates may have been based on forward looking costs, the PSC's determination indicated that they were based on embedded costs, which do not necessarily comply with the new services test."[36] Verizon is, moreover, correct that the remand would only apply the new services test as it existed on April 15, 1997, as Supreme Court rejected complainants' argument that later FCC decisions should be applied. Further, Verizon also seems correct that, in principle, the remand directive should not be difficult to fulfill, as it requires only a comparison between the preexisting rates at issue and the relevant incremental cost data to show whether the rates are supported by forward looking costs.[37]

Complainants' request for a more expansive investigation on remand is not supported by the New York Court proceedings. The complainants have not focused on the language of the Supreme Court decisions, but argue that we should rely on the Indiana and Davel cases as guidance or precedent. Those cases are inapposite because, in both instances, it was found that the regulatory commission had set the rates subject to a possibility of further examination. Thus, the Davel decision was based partly on a finding that a statutory "just and reasonable" proviso (in §201 of the 1996 Federal Communications Act) defeated any presumption that filed tariffs were valid; but a separate, critical factor was the court's finding of an intention, on the FCC's part, that rates applied after April 15, 1977 would be subject to refund. The majority in the Indiana case found a similar intention on the part of the Indiana commission, and

---

[35] July 31, 2002 Albany County Supreme Court Decision and Order at 19.

[36] Id. at 22.

[37] As a practical matter, however, there may be difficulty identifying the relevant data given the lapse of time since the rates were established.

could affect the FCC's disposition of the petition, Verizon is correct that it would be a waste of resources for us to analyze possible discrepancies between the NST and superseded PAL rates before receiving the FCC's guidance (if any) as to the purpose and scope of such an inquiry.

The question remains, however, whether we should take further action in response to the remand. At this juncture it seems that there is no basis for doing so, as Verizon opposes it and the complainants have offered no sound reason for proceeding. One dispositive consideration is that an FCC ruling on IPANY's petition might render the remand proceeding unnecessary or affect the relief provided in that proceeding; both parties seem to recognize that possibility. We therefore conclude that the prudent course here is to conduct no further proceedings pursuant to the remand until the FCC has issued a final decision enabling us to evaluate how best to proceed.

ACCESS CHARGE REVENUES

Verizon's plant may be categorized as traffic sensitive (TS) or non-traffic-sensitive (NTS), depending on whether the plant's costs vary with usage volumes. To comply with the New Services Test (NST), payphone rates must be designed to avoid a double recovery of NTS costs that Verizon already is recovering once through carrier access charges approved by the FCC or through the federal access charges' intrastate counterparts approved by this Commission.[39]

In their comments on the advisory staff white paper, the complainants acknowledged that the white paper would properly recognize payphone revenues generated from one type of access

[39] Access charges were devised as a new source of cost recovery for the Bell operating companies, in lieu of the toll rate system that had prevailed until the 1984 AT&T divestiture. In New York, the intrastate access charge regime for recovery of intrastate costs was designed initially in Case 28425, Impact of Modification of Final Judgement and FCC's Docket 78-72. There and in subsequent cases, we developed intrastate access charges similar in purpose and design to the interstate charges designed by the FCC.

revenue source potentially available to reduce PAL rates is the SLC.[43]

There is no dispute that the PICC's availability for PAL rate mitigation, as authorized by the FCC's Common Carrier Bureau in the first Wisconsin order, ceased when the full Commission in the second Wisconsin order expressly modified that aspect of the Bureau's decision.[44] Thus the only remaining question is whether PAL rates may be offset by CCL revenues.[45]

To begin, the complainants claim that the Bureau's decision in the first Wisconsin order was modified or reversed by the full FCC in the second Wisconsin order only insofar as the FCC removed PICC revenues from PAL rate calculations. They argue that, because the FCC in the second Wisconsin order expressly upheld the Bureau's recognition of SLC revenues and expressly disallowed the Bureau's recognition of PICC revenues, the FCC must have intended tacitly to leave undisturbed the Bureau's decision that CCL revenues should be used to mitigate rates in the same manner as SLC revenues. The complainants further suggest that we need not design intrastate access charges strictly analogous to the system of interstate access charges constructed by the FCC. Thus, according to the complainants, even if the FCC had intended to disallow CCL revenues in the PAL rate calculation--so as to reverse the Bureau by implication--the FCC's decision would not preempt us from following the Bureau's lead and recognizing CCL revenues in the same manner as SLC revenues when setting intrastate rates.

Verizon responds, and we agree, that one cannot reasonably read the second Wisconsin order as complainants propose. The order's clear purpose is to review the Bureau's

---

[43] Matter of Wisconsin PSC, CCB/CPD No. 00-1, released January 31, 2002, supra ("second Wisconsin order"), ¶61. That order modified a prior decision, released March 2, 2000 in the same proceeding ("first Wisconsin order"), which had stated that all three types of revenue should be available as PAL rate offsets.

[44] First Wisconsin order, ¶12; cf. second Wisconsin order, ¶60.

[45] Unlike the interstate CCL set by the FCC, which has no rate impact because it has declined to zero, the intrastate CCL continues to generate a revenue contribution.

In its compliance filing, Verizon initially described the CCL charge as a "source of contribution to a broad range of Verizon's services," as distinguished from a contribution to PAL loop costs.[47] The company's characterization has led to an exchange of arguments about issues that are not germane, such as whether Verizon's intrastate services as a whole are profitable; whether the company's intrastate return can properly be calculated without including revenues from broadband access charges, inside wire maintenance, and wireless services; and whether CCL revenues may properly be used to subsidize flexibly priced non-basic services. These considerations fail to address the overall purpose of access charges such as the CCL which, as noted, were established to recover all the historic costs formerly recoverable through toll charges rather than the incremental cost of specific plant such as PAL lines.

For argument's sake, we can accept for the moment the complainants' perspective that the design and magnitude of intrastate access charges remain open to debate as long as Verizon's financial condition continues to change for better or worse. Even then, however, in asserting that the basic purpose of the CCL should shift to recovering specific loop costs within the framework of the NST, complainants "prove too much." If, as their argument implies, the NST were fundamentally inconsistent with the scheme of access charges adopted for recovery of residual costs in the aftermath of divestiture, that conflict long since would have been addressed in post-divestiture proceedings other than this case. Most notably, it did not arise in the second Wisconsin order where the FCC directly considered in detail the use of access charges as cost offsets. Instead, rate litigation since divestiture has established no authority for the complainants' proposition that the NST precludes the continued use of access charges for general cost recovery as intended at the time of divestiture.

Finally, the complainants assert that the failure to recognize CCL revenues as a cost offset violates the NST by

[47] July 31, 2006 letter, supra, p. 2.

TARIFF MODIFICATIONS

In their comments on Verizon's compliance filing pursuant to the Rate Order, the complainants propose that we modify the new PAL tariffs in two respects. First, they note that Verizon's calculation of the tariffed rates "is static" insofar as it incorporates a fixed value to represent the cost offset related to EUCL (i.e., SLC) revenues.[50] The complainants' proposed remedy is too broad, insofar as PAL rates would vary automatically if the EUCL were modified or if it were supplanted by newly created access charges. Not all such changes should be implemented automatically, when no similar system is in place for recognizing the many other cost elements that may vary after the tariffed rates have taken effect; instead, any cost and revenue changes materially affecting the PAL revenue requirement are more properly addressed in a new, comprehensive rate analysis.

Nevertheless, the complainants are correct that the intent of the Rate Order was to provide an offset reflecting the prevailing level, rather than a fixed amount, of EUCL revenues. Indeed, that intended result presumably has been achieved through a billing arrangement, implemented pursuant to the July 2006 compliance filing, whereby Verizon charges PSPs whatever amount may be needed to recover any difference between the EUCL charge and the total rate shown in the tariff.[51] Thus, an increase in the EUCL charge will automatically cause a countervailing decrease in the amount collected independently of the EUCL, as the complainants advocate.

However, the mechanism for maintaining such equilibrium is not sufficiently specified in the compliance filing. A related concern is that the PAL rates established in the Rate Order are not subject to flexible pricing, and the compliance

[50] Roland letter dated August 15, 2006, supra.

[51] For example, if the monthly Basic PAL rate of $21.47, shown in the tariff, reflects a supposition that Verizon will collect a EUCL charge of $6.86, the company should charge the PSP an additional $14.61 to make up the difference. Hypothetically, if the EUCL were to increase by 20 cents to $7.06, the $14.61 non-EUCL component of the bill would be reduced correspondingly to $14.41.

3. On the basis of the comments filed pursuant to notice issued in these proceedings August 3, 2006, the Rate Order is modified to revoke the requirement that Verizon include in its PAL rates a cost offset on account of revenues from Carrier Common Line charges, and the comment phase pursuant to the August 3, 2006 notice is so concluded.

4. Verizon is directed to file, no later than 30 days from issuance of today's order or as the Secretary may otherwise prescribe, to take effect on a temporary basis on 30 days' notice thereafter, such tariff changes as are necessary to effectuate Public Access Line rates consistent with the discussion in today's order concerning implementation of the offset for End User Common Line Charge revenues and the inapplicability of the flexible pricing option. The Company shall serve copies of its filing upon all parties to these proceedings. Any comments on the compliance filing must be received at the Commission's offices within ten days of service of the Company's proposed amendments. The amendments specified in the compliance filing shall not become effective on a permanent basis until approved by the Commission and will be subject to refund if any showing is made that the revised rates are not in compliance with this order. The requirement of §92(2)(a) of the Public Service Law as to newspaper publication is waived.

5. These proceedings are continued but shall be closed by the Secretary as soon as the compliance filing has been approved, unless the Secretary finds good cause to continue them further.

By the Commission,

(SIGNED) JACLYN A. BRILLING
Secretary